

SUMMARY ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Lempert Analyst: Christy Keith Bill Number: AB 2095

Related Bills: See Prior Analysis Telephone: 845-6080 Amended Date: 05/30/2000

Attorney: Patrick Kusiak Sponsor:

SUBJECT: Scholarshare Trust Refundable Credit/FTB Report To Legislature Annually Regarding Utilization Of Credit

DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended _____.

X AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced/amended _____.

FURTHER AMENDMENTS NECESSARY.

DEPARTMENT POSITION CHANGED TO _____.

X REMAINDER OF PREVIOUS ANALYSIS OF BILL AS AMENDED May 8, 2000 STILL APPLIES.

OTHER - See comments below.

SUMMARY OF BILL

Under the Personal Income Tax Law (PITL), this bill would allow taxpayers a refundable credit for contributions by a qualified taxpayer to a Scholarshare trust made on behalf of any qualified beneficiary. The credit amount would equal a specified percentage of the amount contributed, determined by the taxpayer's filing status and adjusted gross income (AGI), not to exceed \$500 per qualified beneficiary.

This bill also would require the department to report, to the extent data are available, on the utilization of the credit allowed under the bill.

SUMMARY OF AMENDMENT

The May 30, 2000, amendments made several changes, including:

- Increased the credit percentages;
- Increased the maximum credit from \$200 to \$500;
- Disallowed the credit if the beneficiary's Scholarshare account already equals or exceeds the maximum investment level;
- Added a recapture provision that would require that entire amount of credits claimed in prior years to be recaptured in the year of withdrawal if the amount withdrawn is not used for qualified higher education expenses, as defined; and
- Specified more information that the Scholarshare Investment Board must provide to the Franchise Tax board.

Except for the new revenue estimate, the department's prior analysis of the bill as amended May 8, 2000, still applies. The "Implementation Considerations" and "Departmental Costs" from the prior analysis are provided below.

Board Position:

<u> </u> S	<u> </u> NA	<u> </u> NP
<u> </u> SA	<u> </u> O	<u> </u> NAR
<u> </u> N	<u> </u> OUA	<u> </u> X PENDING

Legislative Director

Date

Johnnie Lou Rosas

6/22/00

IMPLEMENTATION CONSIDERATIONS

1. The department has not administered a refundable tax credit under the PITL since the refundable renter's credit was suspended in 1993. Establishing a refundable tax credit program would impact the department's programs and operations and would require extensive changes to forms and systems.
2. Historically, refundable credits (such as the state renter's credit, the federal Earned Income Credit and the federal credit for gasoline used for farming) have had significant problems with invalid and fraudulent returns.
3. The department would need some time to develop adequate programs and operations to mitigate the potential for fraud and to ensure taxpayers receive the refund amount they are due. However, the operative date of this bill (applying to contributions made on or after January 1, 2000) would make it difficult for the department to put in place necessary programs prior to the time taxpayers could file returns claiming the refund. Specifically, if this bill is enacted in late September 2000, taxpayers could begin filing returns claiming the refund as early as January 2001.

DEPARTMENTAL COSTS

The department's costs to administer this bill are estimated to be \$87,871, including one time implementation costs of \$78,812, for fiscal year 2000 and would increase each year as volumes increase until they reach a maximum of \$267,777 in 2007. It is estimated that this bill would require the department to incur one additional personnel year (PY) in 2000, increasing to a total of 6.1 PYs in 2007.

The costs were calculated using the following assumptions based on information the department received from TIAA-CREF Tuition Financing, Inc., which manages the Golden State Scholarshare program.

- Population of taxpayers would start at 27,000 in 2000 and increase to approximately 350,000 in 2007.
- All filers claiming this credit are assumed to be taxpayers who currently file a return. It is not anticipated that this credit would encourage persons who do not currently file a return to file one just to claim the credit.

Note that if the refundability of this credit results in the credit being a "state public benefit" as discussed in "Policy Considerations" in the April 10, 2000, analysis, the departmental costs to administer the bill could be considerably greater.

TAX REVENUE ESTIMATE

Based on limited data and assumptions discussed below, this bill as amended would result in the following revenue losses under the PITL.

Estimated Revenue Impact of AB 2095 As Amended 5/30/00 [\$ In Millions]		
2000-01	2001-02	2002-03
(\$10)	(\$25)	(\$44)

Estimates assume the bill would be effective with contributions made on or after January 1, 2000, with enactment assumed after June 30.

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

REVENUE ESTIMATE DISCUSSION

As a refundable credit, the amount of credits generated and reported on tax returns would determine the revenue impact of this bill. The May 30, 2000, amendments that contributed to increased revenue losses were (1) increasing specified credit percentages from 10%, 5%, and 2% to 25%, 12.5%, and 5%, and (2) increasing the maximum credit from \$200 to \$500.

Developing the estimate required:

1. Projecting the number of accounts for qualified beneficiaries each year (27,000 in 2000 and growing to 202,500 by year-end 2004);
2. Estimating how qualified beneficiaries were distributed by filing status of taxpayers and AGI class;
3. Calculating an average contribution for taxpayers in each AGI class;
4. Multiplying the average contribution by the specified credit percentage (relative to AGI class) to derive an average credit amount;
5. Summing the calculated credits for each vintage within each AGI class; and
6. Applying a rate to reflect the percentage of credits that taxpayers would actually report on their return.

Liability year estimates were converted to cash-flow estimates above. Cash-flow estimates reflect the ability of some taxpayers to accelerate tax benefits by adjusting their estimated tax payments.

The launch date for the Golden State Scholarshare program was October 4, 1999. As of June 2, 2000, net asset value of the Scholarshare trust totaled \$54 million for the benefit of 11,206 beneficiaries. Dividing the net asset value of \$54 million by 11,206 accounts suggests average contributions per beneficiary of less than \$4,800. TIAA-CREF Tuition Financing, Inc. manages the Golden State Scholarshare program. According to TIAA, based on its experience managing other states' tuition financing programs, first-year contributions generally average on the order of \$3,000 per account.

The number of qualified beneficiaries was estimated at 27,000 by year-end 2000. This estimate is based on actual data to date for the Scholarshare trust. Data indicate that the number of new accounts opened each month is increasing on average an additional 10% over that of the previous month. Future vintages of new accounts are assumed to grow 15% in 2001 and 10% annually thereafter. Additional growth was phased-in to account for the incentive effect of the proposed credit.

Tax return data were used to distribute projected accounts for qualified beneficiaries by filing status and AGI class of taxpayers. For each AGI class, average contributions were estimated at 5% of the mid-point AGI. Average contribution amounts were multiplied by specified credit percentages to derive an average credit for each AGI class. Average credit amounts are grown from one year to the next by 3% to represent future growth in income of eligible taxpayers.

Credits for all vintages were summed. Total credits were increased an additional 10% to account for any individual making a contribution on behalf of any qualified beneficiary. Finally, allowances were made for the percentage of credits that would actually be reported.

BOARD POSITION

Pending.